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BY THE U.S. GENERAL ACCOUNTING OFFICE

**Report To The Honorable William Dannemeyer**

**House Of Representatives**

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ORIGINAL

## Subsidized Postage

Certain types of mail receive a subsidy, or preferred rate. An annual appropriation called "Revenue Forgone" provides this subsidy by reimbursing the Postal Service for the difference between regular rates and reduced rates authorized by the Congress. The two largest users of the reduced rates are nonprofit organizations and magazine and newspaper publishers.

GAO's review shows that material is being mailed at the reduced third-class nonprofit rate to produce benefits for both nonprofit and profit-making organizations. Also, publishers of national magazines benefit from a subsidy provided to promote the dissemination of local news and information, especially in rural areas.



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UNITED STATES GENERAL ACCOUNTING OFFICE  
WASHINGTON, D.C. 20548

GENERAL GOVERNMENT  
DIVISION

B-216683

The Honorable William Dannemeyer  
House of Representatives

Dear Mr. Dannemeyer:

In a January 31, 1984, letter, you and former Representative Tom Corcoran asked us to look for ways to improve mailing practices by nonprofit organizations whose postage rates are subsidized by the Congress. An annual appropriation called "Revenue Forgone" provides this subsidy by reimbursing the Postal Service for the difference between regular rates and reduced rates authorized by the Congress. (See p. 1 of app. I.)

You were specifically concerned about whether mailing lists used by nonprofit organizations were accurate and whether such organizations could make greater use of presort discounts.<sup>1</sup> Nonprofit organizations' use of inaccurate mailing lists and nonuse of the presort discount would cause the revenue forgone appropriation to be higher.<sup>2</sup> We found, however, that an analysis of each mailing would be required to make these determinations. And, because this would take considerable time and staff, our review was, after discussion with your office, redirected to more fully develop information we obtained during our review which showed that

--through agreements with nonprofit organizations, for-profit companies benefit from subsidized third-class nonprofit postage rates and

--publishers of national magazines benefit from the subsidy provided to promote the dissemination of local news and information.

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<sup>1</sup>Lower rates provided for mail submitted to the Service sorted by ZIP Code (5-digit) or by carrier route number.

<sup>2</sup>The amount of the appropriation is based on mail volume and Service costs, which equal regular rates. Inaccurate mailing lists increase mail volume (an incorrect address can make the mail piece undeliverable), and Service processing costs are reduced if a mailer presorts the mail.

BACKGROUND

In establishing the Postal Service in 1970, the Congress felt that certain types of mail should continue to receive a subsidy, or preferred rate. Preferred rates are provided to several categories of second, third and fourth-class mail. Second class preferred rates are available to newspapers and magazines intended for distribution within the county where the publisher's designated office of publication is located, plus nonprofit, classroom, agricultural and small circulation publications. Mailings by authorized nonprofit organizations (third-class mail), educational material sent to or from libraries and schools (fourth-class mail) and materials for use by the blind (free mail) are the other preferred categories. The subsidy is funded by an annual appropriation which totaled about \$801 million for fiscal year 1985. (See p. 2 of app. I.)

The subsidy is essentially open-ended. If the annual appropriation (amount is based on estimated mail volume and the preferred rates authorized at the time) is not sufficient to fully reimburse the Service, the Congress provides additional funds in a subsequent year. For fiscal years 1982 through 1985, this annual reconciling adjustment ranged from about \$17 million to \$162 million. (See p. 2 of app. I.)

The Service has estimated that, to provide the preferred rates in 1986, an appropriation totaling \$981 million would be required. However, the President's budget requested no funds for 1986. Instead, legislation will be proposed that will, as stated in the budget, enable the Service to continue preferred rates for most existing subsidized mailers by increasing the rates of the full ratepayers.

The results of our work, fully discussed in the Appendix I, are summarized below.

THIRD-CLASS NONPROFIT MAIL

The Service's financial records show that third-class nonprofit mail receives about 70 percent of the revenue forgone appropriation. The preferred rate can be authorized for eight types of nonprofit organizations.<sup>3</sup> The records do not, however, disclose the number of nonprofit organizations mailing at the preferred rate or the amount of subsidy provided to individual organizations. The preferred rate for nonprofit mail, presorted to only minimum requirements, is 6 cents per piece as compared to 12.5 cents a piece for non-subsidized mail. There is no limit on the number of pieces that can be mailed by a nonprofit organization. Therefore, the amount of subsidy that a nonprofit organization can receive depends on the volume of

<sup>3</sup>Religious, educational, scientific, philanthropic, agricultural, labor, veterans, and fraternal.

mail that the organization chooses (or can afford) to send. Thus, at the preferred rate of 6 cents per piece, an organization spending \$1 million on postage would receive a subsidy of about \$1.1 million.

#### What may be mailed

The Service's Domestic Mail Manual states that an organization authorized to mail at the preferred rates may mail only its own matter at those rates. Any matter produced for or mailed on behalf of an organization not itself authorized to mail at the preferred rates is prohibited. This prohibition does not, however, preclude the mailing of matter which can produce benefits for both nonprofit and profit-making organizations.

To illustrate how profit-making companies benefit from subsidized postage rates, we used case studies to show how nonprofit mailing authorizations are used to sell seminars, insurance, clocks, and watches. (See p. 5 of app. I.) Such use is not prohibited unless it can be shown, as stated above, that a mailing is produced for or made on behalf of an organization not itself entitled to the subsidized rate. One of our five cases fell into this category. (See p. 6 of app. I.)

Although the use of nonprofit mailing authorizations to sell commercial products is not prohibited, mailing at a reduced rate provides a significant competitive advantage to the users of the authorization. For example, the subsidy provided to mailings by a nonprofit association which offered the sale of insurance underwritten by a private insurance company amounted to about \$705,000 over a 1-year period. (See p. 8 of app. I.)

#### IN-COUNTY RATES

To qualify for subsidized postage called the "in-county" rate, a magazine publisher or newspaper designates the location of its office of publication. The publisher then asks the Postal Service to approve one post office as its original entry post office. Only one office can be designated as the office of publication, and this office and the original entry post office must be located in the same county. The subsidized rate is applied on all copies mailed to addresses within this county.

#### National magazine publishers benefit from subsidized rates

We identified six publishers of national magazines which have designated their Los Angeles offices as their office of publication and the Los Angeles Post Office as their original entry post office. Having both offices in Los Angeles County enables a publisher to maximize its use of subsidized postage

rates.<sup>4</sup> We estimate that the six publishers' mailing costs are being subsidized by about \$3.6 million annually from the revenue forgone appropriation. (See p. 11 of app. I.)

These publishers as well as others are benefitting from a subsidy which was provided as far back as 1851. Our review of the legislative history shows that the Congress originally provided the "in-county" subsidy to promote the dissemination of local news and information, especially in rural areas. (See p. 10 of app. I.) However, the legislative language is not restrictive and the subsidy, which totaled more than \$72 million in 1985, benefits both local and national publishers.

#### AGENCY COMMENTS

In commenting on our draft report, the Postmaster General stated that the report correctly describes circumstances under which for-profit companies benefit from subsidized third-class nonprofit postage rates and national magazines benefit from subsidized in-county second-class rates. The Postmaster General believes that such situations arise out of the current statutory framework, and not because of any maladministration of the statutes by the Postal Service. (See app. II.)

An opportunity to review and comment on pertinent sections of our draft report was provided to organizations specifically identified in the report. Comments received (both oral and written) were considered in finalizing this report.

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We trust that the information provided in this report is responsive to your request. Please let us know if we can be of further assistance.

As arranged with your office, copies of this report are being sent to the Postmaster General; the Director, Office of Management and Budget; and other interested parties. We will also send a copy to former Representative Tom Corcoran.

Sincerely yours,

*W. J. Anderson*

William J. Anderson  
Director

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<sup>4</sup>Los Angeles County has the largest population of any county in the United States.

THE REVENUE FORGONE SUBSIDYINTRODUCTION

The Postal Reorganization Act of 1970 abolished the Post Office Department and established the United States Postal Service. Prior to the reorganization, postage rates were set without regard to costs. Thus, the cost of mail delivery was heavily subsidized from general tax revenues. With the reorganization, however, the Service was made self-sufficient, with users paying for its operating costs.

When it established the Service, the Congress felt that certain types of mail should continue to receive a subsidized, or preferred rate. It provided this subsidy through an annual appropriation called "Revenue Forgone." The appropriation reimburses the Service for overhead costs allocated to the following types of preferred rate mail.

- Second-class: newspapers and magazines mailed and delivered in the county where the publisher's designated office of publication is located, farm technical publications, publications by not-for-profit organizations, and material for classroom use.
- Third-class: mailings by authorized nonprofit organizations and mailings by qualified political committees.
- Fourth-class: books, films, papers, and other educational material mailed by libraries, schools, and museums or mailed to libraries, schools, museums and school book stores by publishers and distributors.
- Free mail: material for use by the blind and certain free balloting material for overseas voting.

After authorizing a continuing appropriation to cover overhead costs, the Congress decided that rates would still accelerate too quickly. It therefore authorized an additional temporary subsidy to ease the transition from heavily subsidized rates to rates which provide revenue equal to direct operating costs. A 16-year phasing schedule for providing these additional funds will expire in fiscal year 1986.

The Reorganization Act, as amended, also provides an annual after-the-fact reconciling adjustment to reimburse the Service for the difference between estimated and actual costs. The annual revenue forgone appropriation is based on estimated mail volume and the preferred rates authorized at the time. If the appropriation does not fully reimburse the Service, the Congress provides additional funds in a subsequent year.

Amounts appropriated

The revenue forgone appropriations for fiscal years 1982 through 1985, as well as the amounts requested in the President's budgets, are shown in the following table. The 1985 revenue forgone appropriation, broken down by mail class, is shown in a table on page 3.

AMOUNT AND TYPE OF APPROPRIATION FOR REVENUE FORGONE

| <u>Type</u>           | <u>1982</u>      | <u>Fiscal year</u><br><u>(\$ in thousands)</u> |                  | <u>1985</u>                  |
|-----------------------|------------------|------------------------------------------------|------------------|------------------------------|
|                       |                  | <u>1983</u>                                    | <u>1984</u>      |                              |
| Phasing               | \$149,948        | \$155,805                                      | \$106,476        | \$140,450                    |
| Continuing            | 527,894          | 615,615                                        | 610,692          | 608,503                      |
| Reconciling           | <u>16,828</u>    | <u>17,580</u>                                  | <u>161,832</u>   | <u>52,047</u>                |
| Total                 | <u>\$694,670</u> | <u>\$789,000</u>                               | <u>\$879,000</u> | <u>\$801,000<sup>a</sup></u> |
| President's<br>budget | \$500,000        | \$500,000                                      | \$400,000        | \$452,047                    |

<sup>a</sup>The Service has requested a supplemental appropriation for \$168,620,000 because of rate increases effective in February 1985.

REVENUE FORGONE APPROPRIATION FOR FISCAL YEAR 1985  
(\$ in thousands)

| <u>Class of service</u> | <u>Phasing</u>   | <u>Continuing</u> | <u>Total</u>     |
|-------------------------|------------------|-------------------|------------------|
| Second-class:           |                  |                   |                  |
| In-county               | \$ 6,982         | \$ 65,101         | \$ 72,083        |
| Nonprofit               | 34,465           | 24,836            | 59,301           |
| Classroom               | 276              | 4,753             | 5,029            |
| Regular-rate            | <u>8,405</u>     | <u>9,199</u>      | <u>17,604</u>    |
| Total                   | <u>\$50,128</u>  | <u>\$103,889</u>  | <u>\$154,017</u> |
| Third-class:            |                  |                   |                  |
| Nonprofit               | \$81,761         | \$429,472         | \$511,233        |
| Fourth-class:           |                  |                   |                  |
| Library rate            | 8,561            | 41,196            | 49,757           |
| Free for blind, etc.    | <u>-</u>         | <u>33,946</u>     | <u>33,946</u>    |
| Total                   | <u>\$140,450</u> | <u>\$608,503</u>  | <u>\$748,953</u> |
| Reconciling adjustment  |                  |                   | <u>52,047</u>    |
| Total                   |                  |                   | <u>\$801,000</u> |

For fiscal year 1986, the Service has estimated that the volume of mail authorized to receive preferred rates will result in a subsidy totaling \$981 million. The President's budget requested no funds for 1986. Instead, the budget states that legislation will be proposed to enable the Service to provide preferred rates for most existing subsidized mailers by increasing the rates of the full ratepayers.

OBJECTIVES, SCOPE, AND METHODOLOGY

Representative William Dannemeyer and former Representative Tom Corcoran, members of the House Committee on Post Office and Civil Service, requested our assistance in finding ways to improve the efficiency of mailing practices by nonprofit organizations whose postage rates are subsidized by the Congress. We were specifically requested to consider whether large nonprofit mailers could (1) take greater advantage of presort mail rates and (2) reduce the volume of their undeliverable mail caused by incorrect addresses.

To respond to these specific concerns, we obtained information from Service headquarters and regional officials, nonprofit mailers and firms who prepare their mailings, a mailing list

broker, and direct mail marketing firms. At the Philadelphia Post Office, we obtained information on a sample of 52 mailings which were not presorted by the nonprofit mailers. The mailings were selected judgmentally (various sizes) from 368 nonprofit mailings which were accepted by the post office during the week of February 6, 1984.

Our examination of the above mailings and postal records and our discussions with postal officials, mailers, and other industry officials disclosed that an analysis of each mailing would be required to determine if nonprofit mailers could (1) presort more of their mail and (2) use more accurate mailing lists. Because considerable time and staff would be required to make these determinations, our review was, after discussion with Congressman Dannemeyer's office, redirected to more fully develop information which showed that (1) for-profit companies as well as nonprofit organizations were benefiting from the subsidy provided by the Congress for nonprofit organizations and (2) mailings by large publishers were being subsidized by the revenue forgone appropriation. To respond to an interest in these two areas we:

- Developed case studies of commercial promotional mailings at the nonprofit rate. For these cases, we obtained information from Service files and interviewed officials of some of the private companies or their attorneys.
- Researched Congress' intent in authorizing preferred postage rates for magazines and newspapers mailed within a county. For six publishers who have designated Los Angeles as their known office of publication and the Los Angeles Post Office as their original entry post office, we estimated for a 1-year period the subsidy applicable to 27 of their publications. We discussed the designation of Los Angeles as the location of an office of publication with officials of four of the publishers.

Our work, supplemented by results of audit work done by the Postal Service's Inspection Service, was done in accordance with generally accepted government auditing standards.

#### NONPROFIT MAILINGS

Third-class nonprofit mail receives about 70 percent of the revenue forgone appropriation. The Service's Domestic Mail Manual lists eight types of nonprofit organizations which can qualify for preferred rates: religious, educational, scientific, philanthropic, agricultural, labor, veterans, or

fraternal. To receive the subsidized nonprofit rate, an organization must apply for authorization at each post office where mail is to be deposited. Nonprofit organizations can have an unlimited number of mailing authorizations. Applications are reviewed by the Mail Classification Center responsible for a specific area. According to Center employees, very few applications are disapproved. Service records show that more than 300,000 authorizations have been issued.

Postal Service headquarters, subsequent to a report by the Service's Inspection Service, initiated two projects: identification of inactive authorizations and reverification of organizations' eligibility to mail at the nonprofit rate. As of January 1985, more than 29,000 inactive permits had been revoked for non-usage and, of the 180 authorizations selected for reverification, 93 of 146 reviewed to date were revoked because they no longer qualify for nonprofit mailing privileges.

FOR-PROFIT ORGANIZATIONS  
BENEFIT FROM NONPROFIT  
SUBSIDIES

The Service's Domestic Mail Manual states that an organization authorized to mail at the preferred rates may mail only its own matter at those rates. Any matter produced for or mailed on behalf of an organization not itself authorized to mail at the preferred rates is prohibited. This prohibition does not, however, preclude the mailing of matter which can produce benefits for both nonprofit and profit-making organizations.

Both we and the Inspection Service found that nonprofit organizations have entered into agreements with for-profit organizations which result in large quantities of commercial-type promotional material being mailed at the preferred rate. We found that such arrangements have been used to sell seminars, insurance, and commemorative clocks and watches. The following case studies demonstrate different types of arrangements between nonprofit and profit-making organizations.

Seminars

The seminar business depends on direct mail marketing to attract participants. A survey of the business by a seminar producer, Dominick Schrello, Ph.D., estimated that selling expenses take about one-third of every revenue dollar.

In his book, *The Seminar Market*, Dr. Schrello states:

"Presently, . . . significant postal rate discount gives nonprofit organizations a tremendous advantage compared to others in the public seminar market place.

. . . As a result, some companies have created joint ventures and affiliations with nonprofit organizations."

Dr. Schrello's survey of the business showed that in 1980, 18 organizations accounted for about one-third of the market. Of these, eight were organized as nonprofit organizations or doing business mainly through nonprofit organizations. Dr. Schrello reported that the largest nonprofit seminar producer mails more than 60 million promotional pieces annually. At 1984 rates, 60 million pieces mailed at the nonprofit rate would result in a subsidy of about \$3.5 million.

A for-profit  
seminar producer

A private company furnished us information which led us to a for-profit company that has been designing and administering seminars for nonprofit organizations for at least 10 years. The promotional material mailed under nonprofit authorizations indicated that the seminars were sponsored by a college or university. The mailing authorizations had been issued to the college or university with the seminar producer acting as their agent.

We contacted one of the sponsoring organizations. The president of the college told us that the college agrees to sponsor a particular seminar after reviewing the proposed promotional brochure. The brochure includes a letter on college stationery describing and endorsing the seminar, an outline of the course curriculum, and credentials of the instructors.

The seminar producer furnished us a copy of the seminar management agreement with the college. The agreement states that the seminar producer will, subject to the college's direction, provide management services which include preparation of course material, selection of instructors and seminar locations, collections of fees, and payment of bills. The agreement also provides that the college will receive a share of profits but will make no contribution for any losses which may be incurred.

At our request, Service headquarters officials reviewed the use of nonprofit mailing authorizations by the seminar producer. The Service concluded that the material being mailed by the seminar producer was not eligible for mailing at the nonprofit rate. The Service determined from information furnished by one of the sponsoring organizations that the mailings were being made on behalf of an organization not itself authorized to mail at the preferred rates. The Postmaster of the responsible post office was told not to accept any nonprofit mail from the seminar producer.

The seminar producer told us that they mail 8 to 9 million brochures annually for nonprofit organizations at the preferred rate. This volume of mail would result in a subsidy of about \$500,000. Service records do not show, by authorization number, total pieces mailed.

Nationally recognized  
business school

A nationally recognized business school conducts seminars on a wide range of business-related topics throughout the United States. These seminars are open to the business community and are extensively advertised, using nonprofit rate postage. During 1983, approximately 125 seminars were held. The school estimates that about 10 million pieces of promotional mail were mailed at the nonprofit rate. The subsidy provided to 10 million pieces would have been about \$580,000.

The school has an ongoing arrangement with a New York City for-profit firm whose business is professional education. This firm handles all administrative arrangements for the seminars. It does market research, selects seminar locations, arranges for printing of the brochures, provides mailing lists, and mails the promotional material. In addition, it collects all fees and pays all costs associated with the seminars. All course materials are developed by the instructors who all have some type of employment relationship with the school.

In 1977, the Service investigated the arrangement between the school and its New York partner. The Service found that the New York firm was paid a fee (a percentage of receipts) after deducting seminar expenses and a guaranteed payment to the school. The Service concluded that the degree of control the school had over the seminar made the mailings eligible for the subsidized postage rate.

Eastern university

An eastern university operates an active ongoing Center for Professional Development and uses nonprofit postage rates to promote its various seminars. The Center is geared to the interest of various professional groups in a local area. According to the Center Director, the university develops and produces about 75 percent of its seminars and it receives assistance in developing the other 25 percent from a for-profit seminar consultant. The university does not believe it has the capability to keep up with all the current trends and interest in the seminar field. Therefore, it obtains such assistance from the consultant.

Administratively, the consultant advises on topics, selects mailing lists, prepares advertising brochures, contracts for printing, and at the university's direction, arranges for mailing under the university's nonprofit authorization. The university is the official sponsor of the program and controls all topics, fees, speakers, meeting facilities, and enrollment lists, and receives all seminar receipts. The Center Director also told us that the seminar consultant's name and organization do not appear anywhere in the promotional materials, and its affiliation plays no role in attracting participants. The consultant is paid a fee for services.

We met with the attorney for the consultant. He stated that his client does act as the university's agent and that similar arrangements have been made with other schools. The consultant had given the Service a pro forma agreement to determine informally whether mailings made under the agreement would qualify at the preferred rate. The Service told the consultant they would.

#### Sale of insurance

Mailing made by a nonprofit association to solicit new members also offered to members of the association a health insurance plan underwritten by a private insurance company. Millions of pieces of such material have been mailed at the nonprofit rate. Applications for insurance are mailed to the association which, according to the association's attorney, receives an administrative fee for processing the applications.

In October 1982, the Service revoked the association's authorization to mail at nonprofit rates from the Philadelphia Post Office. The revocation was based on an opinion that the association's current activities were not primarily directed to the stated purpose for which it was formed; that is, to engage in educational or philanthropic activities. The Service concluded that the primary purpose was to sell insurance, not to educate. The association appealed the Service's decision. While the appeal was pending, the Service held in escrow the difference between the regular rate paid by the association and the nonprofit rate for each piece mailed by the association at the Philadelphia Post Office. For a 1-year period, the difference totaled about \$705,000.

The appeal was filed in the United States District Court, Eastern District of New York. When it became apparent that the District Court was prepared to grant the nonprofit association a preliminary injunction against the revocation of its permit, the Postal Service consented to the referral of the matter to a Service Administrative Law Judge. Prior to a hearing before the Judge, the association furnished additional evidence to

substantiate its educational activities. After considering this evidence, the Service reversed its position and the Judge dismissed the case on October 13, 1983. The amount held in escrow was returned to the association.

The Service reversed its earlier position concluding that even though the association was offering the sale of insurance as a means of attracting new members, this did not substantially change the primary purpose for which the association was formed and operated.

In commenting on our draft report the association's attorney questioned the accuracy of statements that the association (1) has an arrangement with a private insurance company, (2) receives a commission for each policy sold, and (3) sponsors the sale of insurance by mailing "sales material."

By letter dated April 3, 1985, the association's attorney informed us that:

"\* \* \* The organization does not 'sponsor' the sale of insurance. It is true that the organization makes mailings at the special third class bulk non-profit rate of postage to attract new members to the organization. The organization offers various member benefits, one of which is the availability of insurance. Many nonprofit organizations afford their members the opportunity to purchase insurance. The organization is thus not alone in this regard. No member is required to purchase the insurance and thus it is incorrect to state that the organization 'sponsors' the issuance. The mailings generate new members for the organization and therefore are properly mailed at the preferred rate. Any contrary inference in your report is incorrect."

Our characterization of the mailings made by the association and how it receives funds from insurance related activities has been changed as described by the association's attorney. We have also provided, as requested by the attorney, additional information on the amount of subsidy (\$705,000) received by the association during a 1-year period. (See p. 8.)

#### Sale of clocks and watches

Alumni associations are mailing brochures promoting the sale of commemorative clocks and watches manufactured by well-known companies. The clocks and watches are uniquely identified with the individual school seal and are offered exclusively to alumni of the school and parents of enrolled students. Three organizations directly benefit from the subsidized postage rate: the alumni association, the distributor, and the manufacturer.

A specimen contract obtained from Postal Service files shows that the distributor was designated as an agent for the alumni association. The contract stated that the association would provide address labels, an official letter and envelope to be reproduced by the distributor for the sales promotion, and a copy of the school seal. The contract specified that the association would reimburse the distributor for postage and mail preparation costs.

The commemorative clocks and watches are ordered from the distributor. According to the contract, the association receives, from the proceeds, a royalty on each clock and watch sold, after a specified number are sold to recover sales promotion costs, which would include postage paid by the distributor.

The Service has determined that the principal/agent relationship established by contract makes the promotional material eligible for mailing at the nonprofit rate.

The above information was based on the specimen contract used by the Postal Service to make the above eligibility determination and promotional material received by GAO staff members. We had no discussions with alumni associations or the distributor.

#### IN-COUNTY RATES

The revenue forgone appropriation also provides a subsidy to second-class mail which originates and is delivered in the county where the publisher's designated office of publication is located. For fiscal year 1985, the Congress appropriated \$72 million for this "in-county" subsidy which benefits both large national publications and small local ones.

Our analysis of legislative history dating back to 1851 shows that the Congress originally provided the subsidy to promote the dissemination of local news and information, especially in rural areas. The authorizing legislation has remained unchanged since 1967. At that time, the Chairman, House Post Office and Civil Service Committee, described in-county rates as "the rates that are applicable to small-town newspapers." However, the legislative language is not restrictive, and large national publishers are eligible for the subsidized rates. In some instances, publishers have maximized this benefit by designating Los Angeles as their known office of publication. Los Angeles County has the largest population of any county in the United States.

To qualify for the in-county rate, a publisher designates a known office of publication and has the Service approve one post office located in the same county as the publisher's original

entry point. Publications entered at the original entry post office and delivered in the county receive the in-county rates.

IN-COUNTY SUBSIDY PROVIDED TO  
NATIONAL SECOND-CLASS MAILERS

We identified 6 national publishers who have designated Los Angeles as their known office of publication for 27 magazines which are sold nationally. Originally, four of the six publications' known offices of publication were located in New York, one was located in Chicago, and one had not formally designated a known office of publication. By designating Los Angeles as their known office of publication, the publishers substantially increased their use of subsidized rates. We estimate the subsidy at about \$3.6 million annually for the six publishers.

The following is an example of how a publisher designated an already existing Los Angeles office as its known office of publication in order to maximize its use of in-county rates.

Entertainment-oriented publisher

The corporate headquarters and main editorial offices of this large entertainment-oriented publication are located in the suburbs of a major eastern city. The paid subscription circulation of this weekly magazine is approximately 8 million.

Before August 1983, the magazine did not mail at the in-county rate. In July 1983, the publisher applied to the Los Angeles Post Office for original entry privileges and designated its already established Los Angeles business office as its office of publication. The publisher told us that this was done to take advantage of the in-county rates. Original entry privileges at the Los Angeles Post Office were granted in August 1983. Copies designated for delivery in Los Angeles are printed in San Jose and trucked to the Los Angeles Post Office for entry. No changes were made in the operations at the Los Angeles office.

By designating its Los Angeles office as the office of publication, the publisher was able to take advantage of the in-county rate for all copies mailed to Los Angeles County addresses. Based on the number of copies mailed in June 1984, this publisher's mailing costs are being subsidized by about \$1.6 million annually.

By letter dated April 4, 1985, the publisher informed us that approximately 75 percent of the content of the magazine relates directly to Los Angeles County local news and information, thereby meeting one of the congressional purposes in authorizing the "in-county" subsidy. (See legislation history on p. 10.)



THE POSTMASTER GENERAL  
Washington, DC 20260-0010

March 22, 1985

Dear Mr. Anderson:

This refers to your proposed report entitled, "Subsidized Postage."

The report correctly describes circumstances under which for-profit companies benefit from subsidized third-class non-profit postage rates and national magazines benefit from subsidized in-county second-class rates.

These situations arise out of the current statutory framework, and not because of any maladministration of the statutes by the Postal Service.

For-profit companies benefit from subsidized third-class non-profit rates through arrangements whereby they provide mail related services for non-profit organizations. These services are generally in areas relating to fund raising, continuing education and the like, activities which revenue forgone appropriations are intended to support. There are occasional borderline cases in such arrangements, and the report discusses some, but we would like to stress that these are the exceptions. In the preponderance of cases, the arrangements are clearly in keeping with the intent of the current statutes.

Similarly, under the present statutes, the revenue forgone appropriation for within-county rates is apparently intended by Congress to benefit all second-class publications. As the report itself notes, the legislative language is not restrictive. A large national magazine is eligible for the subsidized rate in the county where its office of publication is located. If a national second-class mailer chooses to designate its Los Angeles office as office of publication in order to maximize its use of the subsidized rate, there is nothing in the statute to prohibit such action.

We appreciate your giving the Postal Service an opportunity to comment on your report.

Sincerely,

Paul N. Carlin

William J. Anderson  
Director, General  
Government Division  
U.S. General Accounting Office  
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